

General Information Letter: Activities of independent contractors conducted in Illinois on behalf of the taxpayer may cause the loss of protection under Public Law 86-272.

January 24, 2005

Dear:

Your letter to Deputy Chief Counsel Paul Caselton, dated January 3, 2005 has been referred to the undersigned for a reply. Department of Revenue ("Department") regulations require that the Department issue only two types of letter rulings, Private Letter Rulings ("**PLRs**") and General Information Letters ("**GILs**"). **PLRs** are issued by the Department in response to specific taxpayer inquiries concerning the application of a tax statute or rule to a particular fact situation. A **PLR** is binding on the Department, but only as to the taxpayer who is the subject of the request for ruling and only to the extent the facts recited in the **PLR** are correct and complete. **GILs** do not constitute statements of agency policy that apply, interpret or prescribe the tax laws and are not binding on the Department. For your general information, the regulation governing the issuance of letter rulings, 2 *Ill. Adm. Code Part 1200* regarding rulings and other information issued by the Department, can be accessed at the Department's website. That address is www.revenue.state.il.us/legalinformation/regs/part1200.

The nature of your question and the information provided require that we respond only with a **GIL**.

In your letter you state in part as follows:

We are hereby requesting a determination of income tax nexus for the above named taxpayer. COMPANY is a Wisconsin Subchapter S Corporation. Their business activity is retail furniture sales to customers located in southeastern Wisconsin and northern Illinois.

Specific facts relative to a presence in Illinois are as follows:

- ?? COMPANY advertises its CITY location in several northern Illinois county phone books, as well as television, radio and newspapers;
- ?? COMPANY hires an independent contractor to perform repairs in Illinois on furniture sold to Illinois customers;
- ?? COMPANY hires independent contractors to deliver furniture to Illinois residents;
- ?? COMPANY includes delivery charges to Illinois when invoicing Illinois customers;
- ?? COMPANY collects Illinois sales tax on sales delivered to Illinois customers;
- ?? The shareholders of COMPANY are Illinois residents;
- ?? The shareholders have an office in their home used exclusively for business including purchasing furniture, advertising, office work, accounting, company insurance, and human resources;
- ?? COMPANY exchanges and delivers furniture to Illinois customers with their Company owned vehicle.

The Department only issues a determination of nexus in the context of an audit where the Department's auditor would have access to all relevant facts and circumstances. COMPANY was audited by the Department April, 1997. The purpose of that audit was for sales tax compliance. At the conclusion of the audit the sales

tax classification

RULING

The determination whether a taxpayer has nexus with Illinois is extremely fact-specific. Therefore, the Department does not issue rulings regarding whether a particular taxpayer has nexus with the State. However, general information regarding nexus with Illinois for income tax purposes may be provided.

Constitutional Jurisdiction

The United States Constitution restricts a state's power to subject to income tax foreign corporations. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction the state seeks to tax (*Quill Corp. v. North Dakota*, 504 U.S. 298, 112 S.Ct. 1904 (1992)). Similarly, the Commerce Clause requires that a state's tax be applied only to activities with a substantial nexus to the taxing state (*Id.*). Where any part of a foreign corporation's income is allocable to Illinois in accordance with the provisions of Article 3 of the Illinois Income Tax Act ("*IITA*"; 35 ILCS 5/301 – 304), Illinois can demonstrate the connection or nexus necessary to subject a foreign corporation to tax. Therefore, unless protected by the United States Constitution or federal statute (e.g., *Public Law 86-272*, see below), a foreign corporation is liable for Illinois income tax where any portion of its income is allocated to Illinois.

IITA 304 provides for taxable years ending on or after December 31, 2000 that the apportionment factor for a foreign corporation deriving business income from Illinois and one or more other states shall be equal to its sales factor. Section 304(a)(3)(A) defines the sales factor as a fraction, the numerator of which is the total sales of the person in Illinois during the taxable year, and the denominator of which is the total sales of the person everywhere. Department of Revenue Illinois Income Tax Regulations ("*IIT Regulations*") Section 100.3700(c)(1) states that gross receipts from sales of tangible personal property are allocable to Illinois for sales factor purposes if the property is delivered or shipped to a purchaser within this state regardless of the f.o.b. point or other conditions of sale.

Your letter indicates that COMPANY sells furniture to purchasers in Illinois. Because sale of its furniture constitutes sales of tangible personal property, a portion of COMPANY's net income is allocable to Illinois in accordance with the provisions of *Article 3* of the *IITA*. Accordingly, unless protected by *Public Law 86-272*, COMPANY may be liable for Illinois income tax.

Public Law 86-272

Public Law 86-272, 73 Stat. 555, 15 U.S.C.A. 381 (1959) states in part:

No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either or both of the following:

(1) the solicitation of orders by such person, or his representative, in such

State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

In *Wisconsin Dep't of Revenue v. William Wrigley, Jr., Co.*, 505 U.S. 214, 227, 112 S.Ct. 2447, 2456 (1992), the Supreme Court determined that business activities constituting "solicitation of orders" include activities ancillary to requests for purchases. In addition, the Court announced that a taxpayer does not forfeit protection under *P.L. 86-272* by engaging in *de minimis* activities that exceed solicitation of orders. (*Wrigley*, 505 U.S. at 231, 112 S.Ct. at 2458) Accordingly, a taxpayer is not protected under *P.L. 86-272* where it engages in Illinois in business activities that may not be considered solicitation, or activities ancillary thereto, and that are not *de minimis*.

IIT Regulations Section 100.9720(c)(4) lists specific activities considered beyond mere solicitation and therefore unprotected by *P.L. 86-272*. *Section 100.9720(c)(4)(A)* includes in the category of unprotected activities "[m]aking repairs or providing maintenance or service to the property sold or to be sold."

IIT Regulations Section 100.9720(c)(6) provides that *P.L. 86-272* protects certain in-state activities engaged in by independent contractors that would not be protected if performed by the taxpayer's employees or other representatives. Such activities consist of (i) soliciting sales, (ii) making sales, and (iii) maintaining an office.

Your letter indicates that independent contractors repair furniture sold to purchasers in Illinois. Assuming such installation is conducted on its behalf, COMPANY is not protected by *P.L. 86-272* from Illinois income tax. An independent contractor's repair of a taxpayer's tangible personal property sold within this state may not be considered solicitation. Likewise, installation is not an activity that may be engaged in by an independent contractor without the loss of protection under *P.L. 86-272*. Resultantly, COMPANY may be liable for Illinois income tax on all of its income allocable to Illinois in accordance with *Article 3* of the *ITA*.

As stated above, this is a GIL. A GIL does not constitute a statement of policy that applies, interprets or prescribes the tax laws, and it is not binding on the Department. If you are not under audit and wish to obtain a binding private letter ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of *86 Ill. Adm. Code 1200.110(b)*. If you have questions regarding this GIL you may contact the Legal Services Office at (217) 782-7055. If you have further questions related to Illinois income tax laws, visit our web site at www.revenue.state.il.us or contact the Department's Taxpayer Information Division at (217) 782-3336.

Sincerely yours,

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